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Subslug: [Article by Kazuo Nukazawa, managing director, Federation of Economic Organizations: ''Things You Can Contain and Things You Cannot'']

FULL TEXT OF ARTICLE:

1. [Article by Kazuo Nukazawa, managing director, Federation of Economic Organizations: ''Things You Can Contain and Things You Cannot'']

2. [Text] What an irony it would be if at a time when the free economy has at long last proven its superiority over the Soviet-type planned economy, the United States would try to contain the free economy! The ''containment of Japan'' would be synonymous with the containment of a free economy.

3. Foreword

4. I met Mr Fallows only for about an hour when he visited Tokyo 3 years ago under a short-term leadership training program of the Japan Society (in New York).

5. During a chat at that time, he touched on the question of the U.S. burden of defending the free world and asked me in essence how I

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thought about the contention of some Americans that "Japan should assume a certain share of the financial burden." As I remember, my off-hand response was: "Democracy in the United States is based on the idea of 'no tax without representation,' and viewed from the standpoint of this principle, unless Japan is given a say about the U.S. defense policy, there would be no fairness." In retrospect, however, this would give Japan an opportunity to express its views actively when it comes to settling a dispute by force, and Japan would find itself in a rather awkward position under its Constitution; so I think I should have added sotto voce, "Nevertheless Japan would always abstain from expressing its views"

6. In his paper, Fallows presumes that Japan will remain the most valuable single partner of the United States in terms of (1) Japanese-U.S. military arrangements, (2) financial cooperation, and (3) business transaction. In the opinion of the average American, what is most important in relations between countries is security relations, and probably Fallows may view the importance of these terms in the order given above. We have no objection to that. However, we should also give a thought to cooperation in the question of relieving countries with accumulated foreign debts in item (2), namely, financial cooperation.

7. Throughout its history, the United States has alternated between the fatherly image of being the preserver of the prevailing order and the youthful image of the complainant protesting against the prevailing order full of injustices. There have been conflicts between these two images, and these conflicts have given the American intellect stimuli and nourishment. The bright side of this reality is the desire to realize justice, whereas the dark side is the after-the-fact approval of rule by force.

8. In the Fallows paper, we first sense the temperament of the United States as the preserver of the order, determined not to permit Japan, the disturber of the order, from expanding.

9. We then see the face of the United States as the demurrer. Formerly the United States saw Europe as the prevailing order full of injustices. But it is now turning its eyes on what appears to be anachronistic in Japan. What a change. We see how strongly Fallows, who is now a temporary resident of Japan, feels about protesting against the irrational aspects of Japanese society, as well as the boss-dominated aspects of its life which are underlying factors in the rigidity of the market, at least from the standpoint of Japanese consumers.

10. There is something common between these dual approaches. For Fallows, preserving the existing order based on European-American values and breaking up what is irrational in Japanese society are in

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harmony with each other and even complementary to each other. We sense a high moral tone of condemnation and even a sense of mission for reformation, something in common with the erstwhile advocacy of modernization, and there is no room for cultural relativism. On the other hand, Fallows does not know first-hand the fact that once in Japan, there was a generation which angrily felt that 'it is high time for Japan to lead Asia in protesting against the world order centered around the West.'

11. It is hard to put into practice the dictum 'the righteous, be strong,' the teaching of the mother of the late Toshio Doko, former chairman of the Federation of Economic Organizations, but it is harder still to practice the dictum 'the strong, be righteous.' If one regards force as a means for making one's will prevail, he will need self-restraint all the more to refrain from resorting to force, especially when he is not confident whether or not his view is right.

12. In this sense, the present-day United States is on the verge of crisis.

13. Trap of the New View on the Japanese

14. With respect to the conflicting views on the Japanese, Fallows' sketch of the Japanese is correct on the whole. But probably because of the limitations of his linguistic ability, his paper seems to be overly dependent on the criticism of the Japanese by foreigners. As a matter of fact, the originals on which his paper is based have many errors in terms of facts and evaluations. But the Japanese, due to negligence and linguistic limitations, have failed to point out these errors in various forms, such as critical writings in influential foreign journals.

15. It is customary in Europe that observations which have remained unrebutted for a certain period of time are used as the bricks, so to speak, to build the foundation upon which further inductions are based. As a result, the house of cards is being built on the assumption that Japan, 'with an economy constitutionally predisposed to cartels and devoid of free markets, is a xenophobic, development-oriented state led by the government (or marked by a cozy relationship between industry and government)'; a country which has improved the international competitiveness of its industry and practiced mercantilism by pursuing an aggressive targeting policy, and which is the antipode of the United States (or the West) in every aspect. Naturally, the recent Recruit scandal has sprinkled this castle of cards with sequins in the form of a charge that 'Japan is dominated by corrupt money power.'

16. Here, we will digress from the Fallows paper for a while to the arguments used in current Japan bashing, which have the following

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three features in common:

17. A. Pornographic Comparison (or single-factor analysis)
[preceding three words in English]

18. This refers to a lopsided exaggeration of partial truths. To be sure, in the case of Japan, as is the case with other countries, there is hidden in its private parts some truths. Nevertheless, anyone who believes that the private parts contain everything that stands for a woman has a level of intelligence even below that of the adolescent. In a great country with a long history, there are many multidirectional vectors. Accordingly, if one tries to explain everything about it by only collecting single-directional vectors, he can write only an article of ephemeral value. Moreover, one cannot explain everything about a considerably efficient immense national economy on the basis of an induction from the private parts alone, for instance, from the different prices of its articles sold at home and abroad.

19. When pornography directed toward women appears, men will understand why women are mad at the current pornography which is demeaning to them. Would it not be the height of happiness if one were able to see only the most attractive things about foreign countries rather than view their private parts with blinking eyes? We suggest that foreigners make an attempt to practice seeing what beautiful qualities there are in Japan. To be sure, Japan has many such qualities. The Japanese for their part should correct the shortcomings of the Japanese market, even little by little. Admittedly, even well-educated Japanese privately use the word 'geto' or 'ameko' when they refer to Westerners or Americans. They say Japanese are xenophobes, but there are few countries in the world where so many foreign talents appear in commercial messages on TV as in Japan. We want foreigners to see that in a country smaller than California, there are over 1,000 Kentucky Fried Chicken shops and 600 McDonald's hamburger shops.

20. B. View of a Fly in the Toilet (or Jailbird's Sociology)
[preceding two words in English]

21. This view is often found in writings by officials in charge of trade negotiations. A fly in the toilet may believe that all human beings stink, and a fly in the family Buddhist shrine may think that human beings are always sobbing, and a fly in the noodle shop may think that human beings are always making a sipping sound. But what makes a man of intelligence different from a group of juvenile adventurers is that he thinks there may be another aspect of the truth outside the realm of his observation.

22. Negotiators with Japan are always troubled by excessive market

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regulations and its meanness toward foreign firms. If the Japanese side really made the kind of absurd refutations and explanations which Mr Fallows cites, then Japan cannot help but being stigmatized as a cunning temporizing race. But Japan's exports could not have increased to the current level if the Japanese are so untrustworthy, always cheating foreigners as they say. Moreover, if the predilection to cartels is prevalent in Japan as they say, new merchandize could not make its debut on the market, one after another, and the wholesale price could not have dropped 10 percent from the level prevailing 5 years ago.

23. C. Anecdotal Approach (or Anecdotal Economics) [preceding two words in English]

24. It is regrettable that the Fallows paper is not shielded from the effects of his reliance on the originals skewed toward such views. This, in the final analysis, is related to another common feature, namely, an anecdotal approach.

25. Many overseas best-seller type writings by foreign observers follow the stereotype pattern of inflaming low passions in the readers by citing such anecdotes of commercial value as the notorious cases of metal baseball bats and the cumbersome standards for ski equipment (one foolish Japanese blurted out that snow in Japan is not like snow in Europe, and this episode spread throughout the world overnight as a typical illustration of the closed nature of Japanese society), rather than presenting economic and sociological proof based on macroscopic observations. Anecdotes are meaningful in taking the readers by surprise at the beginning of a straightforward economic observation. One Japanese claimed that 'meat is not good for the Japanese because they have longer intestines than Westerners; accordingly, we are opposed to liberalization of meat imports.' This episode may be an interesting subject for a light conversation at the dinner table, but in reality, the beef import quotas as well as beef consumption has increased, and the liberalization of beef imports is in the works. Salad and cheese are served at the table and bread consumption has been popularized. Would it not be a more mature view if one makes the overall observation that the change in the Japanese diet in this half-century has been radical-with no parallel in the world?

26. Well, the Fallows paper says in one breath that MITI [Ministry of International Trade and Industry] has now become a proponent of free trade and in another that the trade policy administered by MITI is totally in the nature of mercantilism. This represents a self-contradiction resulting from his failure to make a macroscopic observation.

27. We will first briefly test the validity of his claim that since

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the adjustment of the exchange rates in 1985, and since the subsequent Maekawa Report of 1986, the constitutional makeup of the Japanese economy has remained unchanged.

28. (1) The ratio of the current account balance to the GNP (this is the only figure appearing in the Maekawa Report) had gradually declined to 2.7 percent as of last year from 4.5 percent in 1985. This ratio will continue to decline, even according to the latest maximum upward modifications of Japan's projected 1989-90 current account surplus, including the IMF projection.

29. In addition, the contribution of international payments balance to growth has been a minus in these 3 years. Incidentally, the ratio of exports to the GNP has decreased to 9.3 percent from 13.2 percent in the same period. The amount of exports has also dropped from 42 trillion yen to the 33-34 trillion yen level.

30. (2) The ratio of manufactured imports began to rise sharply from about 30 percent in 1985, reaching 50 percent in 1988. The income elasticity coefficient of manufactured imports is considerably high at 2.5.

31. (3) The elasticity coefficients of Japanese exports and imports have changed quite radically. For instance, according to the latest monthly survey report of the Bank of Japan, the income elasticity coefficient of the volume of U.S.-bound exports has dropped from 3.5 to 2.8, whereas the price elasticity coefficient has increased from 0.57 to 0.97.

32. According to this year's white paper on trade, the income elasticity coefficient of the volume of Japanese imports increased to 1.07 in 1988 from 0.77 before the realignment of the exchange rates.

33. Already in the 3-year period from 1985 to 1988, manufactured imports increased sharply from \$40 billion to \$92 billion. Then, how can the argument that the readjustment of the exchange rates has no effect whatsoever on the Japanese square with this fact? There have been some worrisome periods in the statistics of the past several months. But if the United States should call for containment of Japan on the basis of these unfavorable months, then would it not strengthen the impression of the United States as a sanction-happy country just like a trigger-happy cowboy in westerns? In May there was a report about a drastic shrinking of Japan's trade surplus. The ratio of U.S.-bound exports to Japan's total exports dropped from 38.0 percent in 1986 to 33.9 percent in 1988. It is too much for Japan to handle if the United States extrapolates the trade balance on the basis of the longest postwar U.S. economic boom lasting roughly for 80 months. We are currently testing whether or not these dual factors, namely, the continuing boom in the United States and

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the rapid increase in the export of capital goods accompanying the sharp increase in Japan's direct overseas investment, are sufficient to explain the slow pace in narrowing the trade imbalance between the two countries.

34. Moreover, if you like, I will use a somewhat anecdotal expression. Japan's annual imports from the United States are greater than the combined total imports from the United States by the three leading European countries (Germany, France, and Italy), this in spite of the fact that both the combined GNP and population of these three European countries are greater than those of Japan. We have, time and time again, pointed out these facts to the American ECONOMIST [as published], but it has made no response except to say that "it is because Europe is farther from the United States than Japan is."

35. Things To Learn

36. However, in reality, it may be useless to point out these and other facts.

37. Fallows knew a long time ago this much: macroeconomic factors are responsible for the trade imbalance of both Japan and the United States. In addition, Representative Gephardt and other influential Americans are unanimous in pointing out that even if the Japanese market is fully liberalized, the payments imbalance between the two countries would improve only by \$8 billion, that is, 15 percent of the total imbalance.

38. To begin with, the trade balance in general and the balance of bilateral trade in particular have no economic meaning, and an exchange rate readjustment produces not much effect unless it is accompanied by macroeconomic policy. West Germany's trade surplus also increased from \$25.4 billion in 1985 to \$72.8 billion in 1988 (Japan's trade surplus increased from \$46.1 billion to \$77.6 billion, both on a customs clearance basis), and this accentuates the necessity for a tighter fiscal policy on the part of the United States and the continued expansion of domestic demand on the part of Japan and Germany.

39. I presume what Fallows really wanted to say is that in spite of all this, unless Japan liberalizes its markets and thus becomes the standard-bearer of free trade in the GATT, the United States and the whole world would suffer, and that unless a big country like Japan achieves a highly balanced economy, it would have an adverse impact overseas.

40. To be sure, there are only national treatment and most-favored-nation treatment as far as GATT rules are concerned, and

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introduction of the kind of reciprocity concept as advocated by Fallows--an idea that is valid only in bilateral relations--would undermine the multilateral system. So, what about considering this issue in the following manner of thinking? Suppose trade and investment are completely liberalized between a highly regulated economy (let it be the Japanese economy) and a sparsely regulated economy (let it be the U.S. economy), American firms still would be unable to enter the Japanese market because of the cost of adapting itself to the Japanese regulations, even if it treated in the same way domestic firms are.

41. Needless to say, Japan has not violated the GATT rules in this regard, and Japan can insist that both sides should meet half way. Nevertheless, it will be beneficial to both sides if they endeavor to eliminate controls as much as possible. The gap in the intensity of control produces friction by generating 'positional energy.' Where there are controls, there necessarily will be the cost of administering the controls and the cost of abiding by them (this cost is several times more than the administering cost) and the controls, themselves, would breed corruption and shady deals. The administrative reform was intended not only to improve efficiency but also to make society a better place to live through an enhanced sense of responsibility on the part of each citizen, the self-cleansing function of society, and a wider distribution of power and information. Won't we feel better if we suppress the feeling that we loathe--or we feel shameful to be forced--to correct our shortcomings under outside pressures, or rather if we think that the country that cannot eliminate its fiscal deficit even under worldwide pressures must be more shameful, and that the country that can rectify its economic shortcomings under outside pressures is much better.

42. Is Japan Following Mercantilism?

43. Is mercantilism, that is, expansion of exports and curtailment of imports, possible nowadays?

44. First, the type of mercantilism referred to by Fallows, that is, the type by which 'Spain and Portugal amassed gold,' is impossible unless the value of gold is considerably stable. It is a known fact that the value of gold has been fluctuating considerably, and the ratio of gold stock to the foreign currency reserves in Japan is 1.5 percent, the lowest among the summit nations (the ratio in the United States is 27.3 percent).

45. Although the value of the dollar has fluctuated violently, we may safely say holdings in dollars have been a depreciating asset for these several years except over the recent several months. The foreign currency reserves of the Bank of Japan have markedly depreciated. In brief, in the age of the depreciating key currency,

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ironically mercantilism may become an act of altruism. It may appear that Japan is pursuing real estate buying, but that is not true either. Janeway of THE WASHINGTON POST (on 28 May) said that 'in making investments in the United States (particularly investment in stocks, bonds, and real estate) the Japanese have a persistent tendency 'to buy at a high price and sell at a lower price.'''

46. Given a floating exchange rate system, mercantile measures (export subsidies, import surtaxes, and a quota system) would be neutralized by changes in the exchange rates. When we enforce an import quota system in one sector, it would rebound to the exchange rate, to the detriment of our own export industries. In addition, in a world where capital moves freely, measures to curb imports will result in a higher exchange rate, depriving export industries of their competitive edges, and eventually transferring employment and tax revenues to overseas. In brief, in the modern world mercantilism contains a self-correcting mechanism.

47. If Japan tries to protect its agricultural products, the food industries using farm products as raw materials will be forced out of business and move their bases of operation overseas. As a consequence, Japan will lose employment, tax revenues, and its bases for the development of processing technologies, and the agricultural sector will lose its markets. On the other hand, if subsidies are paid to ships carrying export goods, foreign shipping agents will hire transports at a lower cost than our own ships, dealing a blow to our own shipping industry, which will also come to demand protection. Thus protection would beget protection, and the cost of protection would fall on the shoulders of the proficient industries. In my opinion, the overwhelming role of Japan's industrial policy in quantitative terms has been the transfer of income from the proficient economic sectors to the inefficient sectors (agriculture among others). (This has been the case since the Meiji era, according to various sources, including a study by Professor Teranishi of Hitotsubashi University, and I wonder why foreigners refuse to learn this lesson.) On the other hand, in my view, the most effective industrial policy in qualitative terms has been the stimulation of rationalization efforts on the part of enterprises through gradual liberalization.

48. The model of a 'developmental state' [preceding two words in English] which underlies the Fallows paper, seems to neglect the question of where the financial resources for protection and fostering come from. This will be the first question to be encountered when pursuing a targeting policy and related managing of trade in the United States. If the financial resources for fostering a high-tech industry are to be sought in the corporate income tax, a greater portion of the actual tax revenues will come from proficient and profitable industries, so this will end up transferring resources

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from the right pocket of the proficient industries to their left pocket.

49. Most probably, the relatively more effective part of our industrial policy has been that it has provided a pool of research and development resources and information on overseas markets for enterprises, has spurred the dismantling of equipment in recession-affected industries, and has given enterprises the rational for their investment decisions.

50. In his paper, Fallows points out that Japan has tried to become No 1 in every field. But a comparative advantage means the ranking in the domestic competition for productivity (as pointed out in the 1987 presidential economic message), and it should be noted that it does not mean, as is generally misunderstood, that industry A in our country is more efficient than industry A in the competitor nation. Even if one country can produce more efficiently than its competitor in every industry, national income will increase when it substitutes imports for a certain group of industries.

51. The Japanese economy will become more efficient when the market rigidity of agriculture, distribution, and other heavily regulated sectors is removed. As things stand now, there will be a manpower shortage of 196,000 by 1993 in the information processing sector alone (according to a projection by the financial department of the Federation of Economic Organizations). Naturally, Japan cannot become 'No 1 in everything' as Fallows claims it wants to, even in areas deemed unimportant. To put it bluntly, if the United States stops protecting the textile industry, at an annual cost of \$20 billion to consumers (according to the 1989 presidential economic message), its national income will increase. Now is the best chance to do this, with the unemployment rate at its lowest in 15 years, and in the longest sustained postwar boom. Incidentally, the United States had better do something about its agriculture, which will have more items on the list of restricted imports than its Japanese counterpart in 3 years from now. Moreover, it is shameful that there is a price gap between Japanese goods sold at home and abroad, but it is also odd that the price of American wheat sold in Moscow is lower than that in the United States.

52. Savings and Investment

53. Saving is delayed consumption. In this sense the dollars that Japan has earned are bound to be spent for consumption. It is painful to be criticized only because we have worked hard and saved prudently in accordance with the teachings of Benjamin Franklin, but it is politically desirable to direct our consumption both in its broader and narrower senses toward the United States as much as possible. Observed overall, the United States has advantages in land-intensive

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goods (farm products), in scale, in defense-related equipment for which its government has put forth great efforts; therefore, it is natural for consumption in the narrower sense of the word to be directed toward American farm products, real estate, and arms. As far as military hardware is concerned, it is outside the GATT liberalization requirements. The reason some people in the United States are apprehensive of Japanese investment in real estate and plants in the United States is that such investment is, as the saying goes, the goose that lays golden eggs. On the contrary, some others are of the opinion that investment in real estate is more desirable because stocks and bonds can be sold overnight but real estate cannot be taken to Japan. The argument that Japan 'should buy eggs, not the goose' boils down to the demand that the Japanese save less. In this metaphor, attention should be paid to the fact that the goose (real estate and factories) will remain in the yard of the other party. Moreover, if additional operational resources are created and more eggs are laid as a result of Japanese participation and the quality of the egg yolk improves, then it will be an additional merit of Japanese investment.

54. Fallows says that Japanese firms operating overseas do not hire non-Japanese for managerial posts. However, in view of the fact that the annual income of section and department chiefs of large Japanese firms has already surpassed that of their American counterparts (except for managing directors or higher officers), there will be a stepped up drive to hire more and more non-Japanese in order to save personnel expenditure, including the cost of stationing Japanese employees in the United States. Japanese firms operating in the United States which fail to put outstanding American youths (who choose not to enter the legal profession or Wall Street in favor of Japanese firms) in key posts will most likely be defeated in the whirlwinds of the American market.

55. Fallows also points out the lag in Japan's efforts to foster social overhead capital. But according to data on hand, the ratio of overall public fixed capital formation to the GNP in the past 20 years has been at least 3 times that in the United States and twice that in West Germany, which rose from the ashes like Japan. In the overall-picture Japan looks like it is falling behind now, but it should be remembered that Japan was a late starter.

56. It has only been 3 years since Japan became first in the world in terms of per capita national income in the wake of the readjustment of the exchange rates. Inasmuch as being rich is an idea involving the stock of wealth rather than its flow, they should not hastily complain that the Japanese living standard is not highest in the world now. If Japan is left uncontained, it will improve this also. Needless to say, land is the most important problem.

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57. Possibility of Containment

58. The logic of economics, just like underground water, cannot be contained by a fence or embankment. The water will burst out if we try to contain it by force. There is a movie in which a white and a black break out of prison handcuffed to each other. At first, they curse each other, but they gradually come to cooperate each other from necessity, and then when their handcuffs are removed, they become inseparable. The relationship between Japan and the United States is closer than MAD (mutual assured destruction) ties, and it seems that their relationship is so close that if one side deals a blow to the other, the blow will rebound to its own economy through natural consequences on its financial and service markets as well as the monetary and capital markets, even if the government of the other side takes no retaliatory measures.

59. If the United States tries to shut out imports from Japan by import restrictions, exports from Japanese production bases in Asia and Europe will increase as long as there is a demand in the United States, and Japanese competitors will fill the void. The United States will have to shut out these imports also and end up imposing a worldwide quota system. When this reaches Wall Street, the market will panic.

60. On the other hand, if Japan is so foolish as to act in such a way as to hurt the U.S. economy, its direct investment in the United States ceases to bring in earnings, and a further depreciation of the dollar will deal a great blow to Japanese life and non-life insurance companies and banks (including the Bank of Japan) with investments in American securities. To begin with, investment is an act which depends on a healthy condition of the economy of the other country more than on trade with it.

61. It may be possible to stem the waves of Japan, but it is impossible to contain the tides of NIC's [newly industrialized country] which will appear on the scene one after another. If they are contained, one by one, then what is contained will not be Japan alone but the world economy itself. What an irony it would be if at a time when the free economy has at long last proved its superiority over the Soviet-type planned economy, the United States should try to contain the free economy!

62. If the United States is determined to contain Japan for the sake of the world order, it should do so only after letting Japan cooperate with it in correcting the present state of affairs--compared with Japan, the United States consumes 2.5 times more energy and emits 10 times more SO₂ (20 percent of the global total), the cause of acid rain, and 15 times more NO_x (approximately 30 percent of the global total). Then

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Japan would not haunt the United States.

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